

MEMORANDUM FOR: Mr. Allan Evans
ATTENTION : Mr. Philip Trezise
SUBJECT : Informal Reply to OIR's Comments on CIA/RR IM-383

1. I was very pleased that Phil Trezise felt free to pass copies of OIR comments on the subject paper to me along with copies of Mose Harvey's covering memorandum to you. This gave my people an opportunity to find out the reasoning which lay behind the feeling that seems to be held by OIR that there is basic disagreement between our respective economists in regard to trends in Soviet economic policy. Now I feel that little real disagreement in fact exists and that the obvious differences of view are minor and in part the result of misinterpretation of some of our statements.

2. It does seem to me that Mose Harvey was a little heavy-handed in contesting our unfortunate choice of language in using the word "reversal" when a reading of the remainder of IM-383 clearly supports his contention that Soviet policy continues to emphasize growth of heavy industry even while increasing emphasis on consumer industries.

3. Enclosed are some comments by my people in support of IM-383 and I hope that these will clear up current misunderstandings.

4. If there are additional points which need further attention, I suggest our respective analysts get together.

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Enclosure

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ORR COMMENTS ON OIR CRITIQUE OF IM-383

1. Most of the points contained in OIR's alternative appraisal of the policy shift are identical with the explicit viewpoint of ORR. The following references illustrate this identity. The memorandum reads, "We see in them, however, no evidence of an intention to lessen emphasis either on short term military preparedness or on the steady expansion of the heavy industry base of Soviet power." (page 1). On page 2 of IM-383, "Although the new program involves a substantial decrease in the rate of growth of the military establishment, it probably does not imply any considerable slowing down in growth of Soviet industrial capacity to support war." From page 3 of IM-383, "It seems clear that the increment to consumption will not come out of resources devoted to investment." In some instances, our language and statistics may have been ambiguous enough to justify misinterpretation.

2. Throughout the body of the OIR memorandum, continual reference is made to an alleged basic CIA statement that, "the announced program implied a revision of the Fifth Five Year Plan and reversed..... a 20 year Soviet policy of giving first priority to the development of heavy industry." The clause, "as Malenkov pointed out" was omitted by the dots. While "reversal" may not have been the most appropriate choice of words, the important point is that the sentence referred to a Soviet statement, and was not a CIA conclusion. Reference is made to this alleged CIA conclusion in the introductory OIR paragraph and in paragraphs A 1 h, B 2 a, D 1, and F 3. ORR did not itself assert a dramatic reversal of past trends. On the initial page of our report we provide comparative statistics to show that the growth of the capital goods industries will still exceed that of consumer goods under the revised plan - "The output of consumer goods will increase at an annual rate of about 7.5 percent and that of producer goods at about 10 percent." Inspection of either Table 3 (page 18) or Appendix B (page 41) provides more detailed proof of our position.

3. In paragraph B 1 in discussing our explanation of the reasons for a levelling off of military expenditures in 1953, OIR states, "However, it cannot be assumed that this resulted from pressure arising from plans to expand consumer goods and agricultural production." By this statement OIR has reversed our cause and effect relationship. Actually, all we claimed was "...its ability to raise consumer goods targets is postulated upon a basic decision not to increase substantially the size of the defense establishment." (page 4)

4. In part D (pages 13-14) OIR misinterprets ORR statistics to conclude that the rate of growth in consumption from 1948 to 1952 was considerably larger than will be the case under the new plan. Therefore,

the extent of the change is not only exaggerated but in the opposite direction than the one we hypothesize. "If the Soviet Union had actually achieved such a feat, Malenkov's new program would be completely unnecessary." (paragraph D 3).

OIR cites the following ORR statistics of consumption (paragraph D 2) in support of their statement:

<u>Year</u>	<u>Billion 1951 Rubles</u>	<u>Index 1940 = 100</u>	<u>Index 1948 = 100</u>
1940	451	100.0	120.0
1948	376	83.5	100.0
1950	502	111.1	133.5
1951	541	120.0	143.8
1952	581	128.8	154.5

The statistics are faulty. The 1940 and 1948 figures are derived from a smaller GNP base used in RR/23, thus leading to exaggeration of the growth in consumption. The OIR text does contain a footnote to the effect that the 1940 and 1948 estimates have been slightly revised since publication of CIA/RR 23, but makes no adjustment for the revision. The corrected statistics appear as follows:

<u>Year</u>	<u>Billion 1951 Rubles</u>	<u>Index 1940 = 100</u>	<u>Index 1948 = 100</u>
1940	472	100.0	112.1
1948	421	89.2	100.0
1950	502	106.4	119.3
1951	541	114.6	128.5
1952	581	123.1	138.0

Instead "during the four years preceding Stalin's death consumption increased by over 54 percent or, compared with the last year before the war, by nearly 29 percent" and "despite a rise in consumption by an annual compound rate of 11.5 percent during the period 1948-52" (paragraph D 3); the increase from 1948-52 amounted to 38 percent, an average annual rate of only 7.1 percent. The level in 1952 was 23 percent over 1940. Furthermore, from 1950, the first postwar year in which per capita consumption reached the 1940 level, to 1953 the average annual rate of growth in consumption was less than 5.5 percent, or less than 4 percent on a per capita basis.

5. OIR states, "...if the CIA figures are correct, the share of consumption in the national product will decline from 54.6 percent in 1952 to 54.4 percent in 1955." (paragraph D 4). The relevant year in the analysis is 1953, since this is the one in which the policy decision was made. Table 4 on page 20 of IM-383 indicates a steady decline of consumption's share from 56.2 percent in 1950 to 54.0 percent in 1953, then forecasts a slight rise to 54.4 percent in 1955.

6. OIR states in paragraphs E 1 - E 4 that our growth rate estimates are too high, claiming that with only a 1-2 percent annual increment in the labor force our high growth rate can only be justified by unfeasibly high productivity increase of 7-10 percent a year. This criticism overlooks the significance of an average annual rate of increase in the industrial labor force of over 6 percent a year between 1948 and 1953. Given this basic statistic, the necessary productivity increases required to support the rate of growth in output are within the realm of possibility.

7. OIR questions the validity of our output indices in paragraph E 5. The restrictions of a secret security classification limit our efforts of support in this regard. However, citation might be made to the study by Turgeon comparing output estimates in the classified 1941 plan and in public speeches. He indicates almost complete identity of estimates in the two sources.

8. OIR in paragraph E 4 illustrates the tenuous nature of ORR aggregate output measures by citing the use of construction machinery output as an indicator of construction machinery production. This use of an indicator is a typical in our GHP index. In most of the sectors at least 80 percent of output is directly represented by physical estimates. The weight of the construction machinery index is miniscule, only 0.6 percent of industry and 0.2 percent of GHP.

9. In paragraph F 1 OIR states, "The CIA report fails to put Soviet promises and plans in proper perspective." In contrast their position indicates "it is clear that the overwhelming proportion of Soviet investment under the so-called 'new program' is still going to heavy industry and the military establishment." Part III A 1 of IM-383 (pages 23-25) and Table 6 estimates the consumer goods industries and agriculture accounted for 15 percent of total investment in 1953 and under the new program in 1954 this proportion would rise to only 18 percent.

10. In paragraph F 3 the memorandum gives an indicator to prove we have over-estimated the resource and priorities effect of the new program on production of capital goods and military end items. "If... total consumer durable produced in 1955 under the new program require only 3-4 percent of probable 1955 steel output, why should there be any significant reduction in military production to accommodate the Soviet consumer?" This figure excludes the steel required to construct the plant and equipment necessary to manufacture all types of consumer goods, durable and non-durable. It also leaves out the new requirements for agricultural capital equipment and flow materials production.

11. In paragraph F 2 a the memorandum points out "The 'official' food products goal for 1955 is given as 169 percent of 1950 in the table on page 26, yet on page 10 and elsewhere the report refers to the Soviet goal as 185 percent." The two estimates are not comparable and our report should have so indicated. The 185 percent figure is an official release. The 169 percent figure represents an aggregation made with ORR weights applied to official physical estimates. The purpose

of the latter was to facilitate a comparison of official goals and ORR estimates of attainments for a specific list of food items. We could not have a valid comparison with an official Soviet aggregate which contained a different set of commodities weighted in an unknown manner.